CPI Competition Policy Institute

April 18, 1997

Chairman Reed E. Hundt
Commissioner James H. Quello
Commissioner Rachelle B. Chong
Commissioner Susan Ness
Federal Communications Commission
1919 M Street, N.W.
Washington, D.C. 20554

Re: *Ex Parte Communication -- CC Dockets No.96-45 and 96-262*

Dear Mr. Chairman and Commissioners:

In the past two weeks, the Commission has received, in *ex parte* presentations, two significant new proposals concerning access charge reform and universal service funding. We are writing to comment on those proposals and express our support for major features of each of them. While we do not agree with every aspect of each plan, **these two compromise proposals offer some very important ideas that should be included in the Commission's decisions on access charge reform and universal service.**

On April 4, AT&T, Bell Atlantic and NYNEX presented a joint proposal to reduce and restructure access charges and fund universal service through a combination of carrier assessments and a new federal end-user charge of $0.75 per line per month. On April 16, a consumer/business group presented a plan to phase down access charges to economic costs over five years, provide high cost support, and fund the Joint Board's recommendation for schools, libraries and other programs without new or increased end-user charges.

In various ways, these two proposals illustrate some very important points about access charge reform and universal service funding:

- **Meaningful access charge reductions can be achieved at the beginning of the process.**

  Each proposal contains significant access charge reductions, effective on July 1, 1997. CPI believes that initial access reductions are a necessary key ingredient in access charge reform. This reasoning is greatly strengthened by the new LEC price cap earnings reports, which show average earnings of 15%, far in excess of the market cost of capital. Clearly, access prices are too high, *even in relation to embedded costs,* and the price cap X-factor is too low for these LECs.

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The proposals (one of which is put forward by two RBOCs) demonstrate that a significant initial reduction can be achieved. The consumer/business groups advocate an initial reduction of $2.9 billion; the AT&T/Bell Atlantic/NYNEX proposal reduces access by $2.2 billion. In each case, this initial reduction can be made either as an adjustment to the price cap formula or as a "policy-based" reduction discussed in Paragraph 232 of the Notice.

- **Significant additional prescriptive reductions in access charges can be made if competition does not produce lower access charges.**

  Many commenters in this docket argue that market forces will not be sufficient to bring access charges to cost and recommend that the Commission make prescriptive reductions. These new proposals show that such prescriptive reductions can be made.

  The consumer/business proposal illustrates how access charges can be reduced to economic costs over a five year transition, in tandem with universal service implementation. The AT&T/Bell Atlantic/NYNEX proposal is more conservative, reducing access charges by the greater of price cap reductions or a percentage of the TIC.

- **High-cost support for large LECs can coincide with reductions in access charges. No new money is needed up front.**

  The consumer/business proposal demonstrates that no new money is needed to support high cost areas of large LECs. Instead, this support can be provided as access reductions occur and after the Commission adopts a cost model. While the AT&T/Bell Atlantic/NYNEX proposal does not address high cost funding for large LECs after July 1, 1998, it does demonstrate that it is not necessary to go beyond the current level of high cost funding at this time.

- **Net consumer benefits can be achieved after full funding for schools, libraries, rural health care, and low-income programs is in place.**

  Each proposal demonstrates that access charge reductions can be structured so that consumers see net benefits, even taking into account full funding for schools and libraries and other programs. Importantly, each proposal also recognizes that funding for schools and libraries will ramp down after initial capital outlays and expenses are completed.

While CPI supports major features of each proposal, there are four issue areas where we may differ with portions of one or the other proposal:

- Universal Service Surcharge

  CPI opposes the AT&T/Bell Atlantic/NYNEX proposal to institute a $0.75 end user charge to fund support for schools, libraries and rural health care. The FCC and the States should treat universal service contributions by regulated carriers as a cost of doing business, to be recovered in the ordinary way — through standard ratemaking mechanisms. For price cap LECs, the universal service obligation could be treated as an exogenous change to the price cap index, applied to the most competitive access services on the originating side. In this way, these LECs will have an opportunity (but not a guarantee) to recover these costs, similar to unregulated providers in fully competitive markets.

- Economic Costs as Basis for Access Charges

  The consumer/business proposal reduces access charges to forward-looking economic costs over a transition period. In contrast, the AT&T/Bell Atlantic/NYNEX proposal does not endorse economic costs as the target for access charges either through prescriptive or market-based means. This is a serious shortcoming of the proposal which limits its applicability to an interim period.

- Responsibility for Non-Traffic-Sensitive Costs

  Access charges should be based on forward-looking economic costs, including a reasonable share of joint and common costs. It is not clear in the consumer/business proposal whether interexchange carriers, wireless carriers and others would continue to bear some responsibility for such joint and common costs as the common loop. As a practical matter, this issue arises only in the later stages of access reductions under their proposal and does not diminish our support for the general structure of the proposal.

- Prescriptive and Market-based Approaches

  CPI shares the skepticism of the consumer/business groups that market forces may not be sufficient to reduce access charges without prescriptive action by the FCC. Nevertheless, CPI believes that, following a significant initial prescribed reduction, market forces should be given a chance to achieve access reductions, under the close scrutiny of the Commission. If access charges fail to move toward economic costs, the Commission should order additional access reductions. The consumer/business group proposal offers a recipe for such reductions.

In conclusion, these two proposals show how the Commission can adopt significant access charge reductions in its orders on universal service and access charge reform. CPI urges the Commission to make such reductions and avoid new or increased end-user charges. Only in this way will consumers realize the net benefits envisioned by the Telecommunications Act of 1996.

Sincerely,

Ronald Binz

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